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The Operation of Islamic banking in Nigeria: A Case of Jaiz Bank plc

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Abstract

Despite strong opposition to the practice of Islamic Banking in Nigeria by those who are either ignorant of its prospects or religiously biased to it, Jaiz Bank which commenced as an interest-free bank in Nigeria in 2012 with only three branches has more than eleven by the end of the year 2013. This paper examined the survival of Islamic banking system in a difficult terrain. The paper appraised the operational system of Jaiz Bank Plc and at the same time, studied the agreement of its operational system with the basic principles of Islamic banking using both analytical and descriptive research methods. The paper identified defaulting in repayment of financing as one of the challenges faced by the bank and suggested that among other things, adequate machinery for checking payment of debts needs to be put in place. It is hoped that if this newly introduced banking practice is sustained, Nigeria will overcome many of its current economic predicaments. However, the sustainability of the system depends on firmness, strong determination and focused objective from the side of Muslims and Non Muslims in Nigeria. The promised land of attaining a formidable and effective interest-free banking may not be reached except qualified and competent Muslim scholars are appointed and retained as members of Advisory Committee to the bank.

Introduction

The foundation of modern institution that mobilizes financial resources from surplus unit and invests them into deficit unit in an attempt to achieve predetermined islamically acceptable social and financial objectives was laid on the notion that commercial banks are needed to cater for the welfare of citizens but the existing conventional banks neither comply with the provision of *sharī'ah* nor relief the citizens of their pangs hence, inherent challenges that are man-made accounted for a modified banking system that is based on the concept of *mudārabah* or profit and loss sharing. The Conference of the Finance Ministers of the Islamic Countries held in Karachi in 1970, the Egyptian study in 1972, the First International Conference on Islamic Economics in Makkah in 1976, and the International Economic Conference in London in 1977 were the result of institutional involvement in Islamic banking¹. This involvement which is later embraced by governments, led to the application of theory to practice in banking system and resulted in the establishment of interest-free banks. The first experiment with Modern Islamic banking was the Myt Gamt savings bank experience in Egypt in 1963 under the leadership of Dr Ahmad El- Naggat followed by that of Dubai in 1975². These banks were established with the objective of

providing an alternative to the conventional interest-based banking in an attempt to cater for the welfare and good living of the citizen in a way that it would help in achieving the socio-economic objectives of the society. An Islamic bank is therefore, committed to do away with disparity and to establish justice in the nation's economic industry as well as to build socio-economic infrastructure and create employment opportunities for members of the society. In Nigeria, efforts towards the establishment of Islamic Bank date back to the 1990s when the idea was first mooted with two licenses granted in 1992. Unfortunately, none could commence operation. The promulgation of the Banks and other Financial Institutions Decrees (BOFID) 24 and 25 of 1991, which replaced the Banking Act of 1969 signaled a new dawn for banking operation in Nigeria³. In 1999, the former Habib Nigeria Bank Limited which later transformed to Bank PHB and currently Keystone Bank started a non-interest banking window with a limited number of *sharī'ah* compliant products⁴ and subsequently, jaiz bank Plc emerged as the first interest free bank in Nigeria.

Jaiz Bank Plc: An Overview

Jaiz International Plc was incorporated on 1st of April, 2003 as a public limited liability company with the opportunity of establishing an Islamic banking institution in Nigeria. The policy of the Federal Government was considered not to be conducive for non interest banks because, with the approval given to *Jaiz* International Plc, it was only able to raise a little over 2.5 billion naira in 2003 out of the 25 billion naira requirement of the CBN⁵. Understanding the situation on ground, the CBN in August 2010 released two new banking models which categorized non-interest banks as specialized banks. These models are the National non-interest bank of capital base of N10 billion with operation in every state of the federation including the Federal Capital Territory (FCT); and the Regional non-interest bank with capital base of N5 billion which shall operate in a minimum of six states and maximum of twelve contiguous states of the federation⁶. With this new banking policy, the major problems of regulatory and supervisory issues are resolved and the problem of capital base is equally managed. The circular defined a Non Interest Financial Institutions (NIFIs) as: "a Bank or Other Financial Institution (OFI) under the purview of the CBN, which transacts banking business, engages in trading, investment and commercial activities as well as provides financial products and services in accordance with *Shari'ah* principles and rules of Islamic Commercial Jurisprudence"⁷ The Framework on Non-Interest Financial Institutions (NIFIs) issued by the Central Bank in January 13, 2011 was followed with the CBN Governor's, (Sanusi Lamido Sanusi) announcement on Monday, June 20, 2011, at a Conference on Islamic Banking in Dakar, Senegal, that it had issued *Jā'iz* International PLC an Approval-in-Principle as the "first Islamic Bank in the country and on 11th November, 2011, *Jaiz* International PLC which was founded

in 2003 received a license from the Central Bank of Nigeria, to operate as a Regional Bank⁸. On 6th January 2012, the institution commenced business as *JaizBank Plc* in offices and branches in Abuja, Kaduna and Kano and as of December 2013, *JaizBank Plc* has its Head Office and two branches in Abuja, two branches in Kano and a branch in each of Kaduna, Gombe, Maiduguri, Katsina, Gusau and Lagos⁹.

The Advisory Committee of Experts (ACE) of *Jaizbank Plc*, during its maiden meeting held on the 19th and 20th October, 2011, resolved that an independent "*Waqf*" type Foundation be established. This gave rise to the formation of the *JaizCharity and Development Foundation* on the 2nd April, 2012, with Registration Number 51511 under the Chairmanship of Alh. Ahmad. S. Maiyaki. Functions of the foundation among others include; building mosques, sinking bore holes, constructing roads, building learning centers and other related capital projects to the community on *waqf* basis¹⁰. The foundation also facilitates agricultural financing and **assists entrepreneurial individuals** and other small scale industrialists through micro credit. As regards health care, the foundation conducts intervention on medical relieve programs and **provides relief materials to victims of accidents or natural disaster** such as flood, earthquake, fire outbreak, civil unrest, etc. **The Foundation** equally renders educational services for the benefit of the community. The basic sources of fund of the Foundation include; direct interest (*riba*) accrued to the bank from its various transactions with other banks and financial transactions; money realized from defaulting investment customers of the bank; fund realized from Blank Documentation; fund realized from income through *zakat* from the Mother Bank; the Bank Account Holders; Corporate organizations as well as individuals, staff of the Bank and the Foundation as well as money realized from the donation and grant of the Mother Bank¹¹. This discussion will now take us to *JaizBank* products which is expected to introduce us to the various products rendered by *Jā'iz Bank PLC*.

Jā'iz Bank Products

Like other conventional banks, *Jaizbank* offers products such as profit sharing (*Muārabah*) product, safekeeping (*Wadī'ah*) product, joint venture (*Mushārah*) product, cost plus (*Murabahah*) product, and leasing (*Ijārah*) product. Out of all these products. The *Muārabah* product appears to have a wider embracement in the society because it covers the savings and deposit accounts that are much patronized even in the conventional banks hence, our discussion will concentrate on this product.

JaizMuārabah accounts include *Muārabah* saving account, *Muārabah* deposit account, hajj savings account and kiddies savings account. The *Muārabah* Saving Account of *JaizBank* is an account that allows customers earn profit on their savings. In this service, the customer enters into a contract based on *Muārabah* with *JaizBank*. In which case, a customer is an Investor

(*Rabbul-Māl*) and the bank is the Manager (*Mudārib*) of the funds deposited by customers and saddled with the responsibility of allocating the funds received from the customers to a deposit pool for investment¹². Popular among the *Jā'iz* savings account is the Specified Investment Account in which the bank receives monies from depositors desiring to appoint the bank

as an agent to investing their deposits in specific projects or in a specified manner on the basis that the bank will receive a part of the net profits realized, but will not be liable for any loss which is not attributable to any violation or fault by the bank. Similar to *Mudārabah* Saving Account is the *Mudārabah* Deposit Account. In this account, funds are invested for a minimum period of 60 days under the principle of *Mudārabah*. The owner of the capital in this arrangement is the Investor (*Rabbul- Māl*) while the bank will be the manager (or *Mudārib*) of the funds deposited in a deposit pool¹³.

JaizHajj Saving Account is a target deposit for customers who intend performing the Holy Pilgrimage. In this special *mudārabah* account, the customer will be entitled to profit share on the deposited amount because just like other *mudārabah* savings, a Hajj Saving Account holder is the Investor (*Rabbul- Māl*) and the bank is the manager (or *Mudārib*) of the funds deposited in the deposit pool and the said deposited money will be managed in accordance with the rule of *mudārabah*¹⁴.

JaizKids Saving Account is a special saving account operated by **JaizBank** with an account opened in a child's name and the parent/guardian acting as a trustee to the account. When the child reaches 18 years of age, he/she may have access to withdraw funds from the account. On agreeing to become a Kids Saving Account holder, a child will enter into the contract of *Mudārabah* with the Bank. Under this relationship, he will be the Investor (*Rabbul- Māl*) and the Bank will be the Manager (or *Mudārib*) of the funds deposited by the child in the deposit pool¹⁵. On agreement to save money into this account, the bank reserves the right to invest the money in a business on behalf of the investor in which case, the investor will be entitled to his share of the profit made from the investment and will equally be prepared to share from a loss incurred if it does occur.

JaizCurrent Account is a Naira current account tailored for customers who carry out frequent transactions and would require unlimited access without any restrictions on withdrawal while enjoying a host of professional services from the Bank. *JaizCurrent* Account can be opened by **Individuals, Sole-Proprietorships, Partnerships, Companies and other registered organizations**. The Bank safely keeps the money for the customer and releases the money to customers at request¹⁶. The Bank on agreement, is investing the money deposited in a current account in an ethical and responsible manner in which case, the principle of *Qard* is implored. In which case, the money

placed into the account is a loan to the bank and the customer is neither entitled to a profit from the business nor is he liable to any loss incurred,

mudārabah is a transaction that is allowed in Islam by consensus of scholars¹⁷. In Islamic economy is a transaction in which two persons co-operate with each other on the basis of partnership, where the capital-owner (*rabbulMāl*) provides the capital and the other party (*mudārib*) puts his management skills into the business¹⁸. The capital-owner is not involved in the actual day-to-day operation of the business, but is free to stipulate

certain conditions that he may deem necessary to ensure the best use of his funds. After the expiry of the period, which may be the termination of the contract or such time that returns are obtained from the business, the capital-owner gets back his principal amount together with a pre-agreed share of the profit. The ratio in which the total profits of the enterprise are distributed between the capital-owner and the manager of the enterprise is determined and mutually agreed at the time of entering the contract before the beginning of the project. In the event of loss, the capital-owner bears all the loss and the principal is reduced by the amount of the loss. It is the risk of loss that entitles the capital-owner to a share in the profits. The manager bears no financial loss unless if caused by negligence or by violation of the contract, because he has lost his time and his work has been wasted¹⁹. *Mudārabah* is the basis of modern Islamic banking on a two-tier basis. Either the depositors put their money into the bank's investment account and agree to share profits with it. In this case, the depositors are the providers of the capital and the bank functions as the manager of funds, or the entrepreneurs seek finance from the bank for their businesses on the condition that profits accruing from their business will be shared between them and the bank in a mutually agreed proportion and any loss will be borne by the bank only. In this case, the bank functions as the provider of capital and the entrepreneur functions as the manager. The rationale behind the principle of *mudārabah* is that in Islam, there is no justifiable reason why a person should enjoy an increase in wealth from the use of his money by another unless he is prepared to expose his wealth to the risk of loss²⁰. Islam views true profit as a return for entrepreneurial effort and objects to money being placed on a pedestal above labour, the other factor in production. As long as the owner of money is willing to become a shareholder in the enterprise and expose his money to the risk of loss, he is entitled to receive a just proportion of the profits and not merely a nominal share based on the prevailing interest rate. The only difference between Islamic banking and interest-based banking in this respect is that the cost of capital in interest-based banking is a predetermined fixed rate, while in Islamic banking; it is expressed as a ratio of profit

There are at least three reasons for considering the *mudārabah* relationship more just than the creditor-debtor relationship of the conventional bank. Firstly, both parties agree on the ratio in which profits will be shared between them hence, it is a game of consent. Secondly, the treatment of both parties is uniform in the event of loss, since if the provider of the capital suffers a reduction of his principal, the manager is deprived of a reward for his labor, time and effort and thirdly, both parties are treated equally if there is any violation of the agreement. If the manager violates anyone of the stipulated conditions, or if he does not work, or is instrumental in causing loss to the business by negligence or bad management, he will have to bear the responsibility for the safe return of the whole amount in question. If, on the other hand, the provider of the capital violates any of the stipulated conditions, for example, by withdrawing his funds before the stipulated time, or by not providing part or full funds at the promised time, etc., he will have to pay the manager a reward equivalent to what he would have earned in similar work.

Notwithstanding the merits of this system, the danger of moral hazards in *mudārabah* where the bank or the *rabbul-māl* bears all the loss and this might prevent the bank from making large investments with an individual *mudārib*²¹. It is equally observed that traditional *mudārabah* system is not a true representative of Islamic spirit because the institution of *mudārabah* can be exploitative. Much would depend on how it is practiced. In particular, one may question the fairness of the arrangement whereby all losses were the result of wrong decision and bad management by the entrepreneur. In the same vein, one may wonder how just it is that the entrepreneur gets nothing for his efforts if no profits are made for reasons beyond his control. To put it quite mildly, there are deficiencies in the traditional *mudārabah* system. Search for alternative arrangement which conform to the Islamic ethical values in both is that which entitles the entrepreneur to wages for services rendered and allows both profits and losses to be shared by the entrepreneur and the owner of capital²².

Challenges of Jā'iz Bank Plc

While it might be unrealistic to overemphasize the benefit one could expect from the adoption of an Islamic banking system and the practice of *mudārabah* in particular, it must be stated that absence of the financier's intervention in entrepreneur's activities in *mudārabah* contracts could certainly generate problem especially if the entrepreneur could not keep adequate record.

Other challenges include the challenge of defaulters in payment. For the fact that interest is not charged on loans taken, some members may fail to pay back the loans they took at when due, this will definitely have a negative effect on the smooth running of the bank because when loans taken are not paid back on time, others may not have a similar opportunity of benefitting from the loan. Except adequate machinery is put in place for debt recovery, the bank may record bad debts.

The challenge of betrayal of trust is equally feared in the bank. Even when it is agreed that *Jā'iz*bank is an Islamic bank, it will be wrong to assume that all those who will be working in the bank will be God conscious just because they are Muslims. Some of those who are engaged in the bank may be products of the corrupt system who can betray the trust reposed on them and act against the oaths they took before Allah and members by mismanaging the money put in their care or using it to their personal advantage.

Except continuous seminars, lectures workshops and training are organized, customers of the bank may have a wrong perception of Islamic finance and conceive it as the same with the western economic system and if they are not adequately oriented, the objective of Islamic banking may not be achieved by *Jā'iz*Bank. Similar to this is the insufficiency of competent and experts in the banking system.

Nigeria is a country with thirty six states and the Federal Capital. For *Jaiz*Bank to be able to operate in the same manner in which other conventional banks operate, it must have branches scattered all over the states with at least a branch in each of the state capital. Up till this time, *Jaiz*Bank has not been able to capture up to half of the nations state and this threaten its national acceptability. The truth however, remains that the financial implication of having branches all over the country may be a burden on the bank but that notwithstanding, at least all Muslim dominated states should have a branch

Phobia on the part of non-Muslims is a serious challenge to the practice of Islamic banking in Nigeria. Ever before the full commencement of *Jaiz*Bank, The CBN was accused of introducing religion into Nigerian banking contrary to the spirit, letter and intendment of Section 39(1) of BOFIA which states: "Except with the written consent of the Governor (a) no bank shall, as from the commencement of this Decree, be registered or incorporated with a name which includes the words "Central" "Federal," "Federation," "National", "Nigeria", "Reserve", "State", "Christian", "Islamic", "Moslem", "Quranic", "Biblical" ²³ If criticism against the system is this much hot, certainly some Christian may have negative attitude to associating with the new development even if not for any reason than for the word "Islamic" that appears on it²⁴.

Prospects of *Jaiz*Bank Plc

The fact that Muslims are beginning to realize the advantages of Islamic banking makes them have a positive attitude towards it. With increase in patronage of the system in Nigeria, it is hoped that the system has come to stay in Nigeria and if it so happened, citizens of this country should be assured that the bank will assist this nation in the building of trust which will be guaranteed in its exhibition of transparency because, it has being asserted that justice which is the basic principle of *Jaiz*Bank, is an essential requirement for all kinds of Islamic financing²⁵. In contrast with conventional banking, Islamic banking looks into moral and ethical values in its banking operations.

Not only will tranquility of mind be promoted by *JaizBank* as against the anxiety which characterizes interest loans of the Conventional Banks, the Bank will equally assist in the creation of more job opportunities in the society because it is not a bank that is after profit alone. After releasing any loan for business, it is in the policy of the bank that there should be staff who monitor the way and manner the loan is being used hence, specialists in the field of such business will be required for proper monitoring of the business in addition to the staff that are engaged inside the bank.

The fact that anybody who takes loan from an Islamic bank is not expected to pay any additional amount above what he has taken, will reduce inflation to the barest minimum in the society. High profit which will burden consumers will not be added to the sale price of commodities bought with loan acquired from *JaizBank*. In a similar vein, *JaizBank* will make money circulate among many people in Nigeria because it will take care of the low income traders who, if not for the existence of the bank, would not have had an access to meaningful loan from a bank for fear of the interest to be paid

Conclusion and Recommendations

This paper has traced the development of non interest banking in Nigeria from the time when it was a window in the conventional banks of the country to the time when *Jā'izbank* was licensed to take off as a full fledge Islamic /non interest bank. Even though the bank offers numerous products, the paper examined the *mudārah* product of the bank and haven identified the prospects and challenges of the bank, it is recommended that;

The bank should retain its connection with those countries that have long being operating the system for deep experience but even then, recognition must be given to the peculiarity of this country among other countries where the system operates in the aspect of multiplicity of religion and hostility of the environment to Islam.

The need for expansion of its branches is imperative for it to gain a desired national and global recognition. It is a fact that establishing a branch is cost implicative but even then, if the management could do its homework properly, some concern governors of the states especially in the northern states of the country will give the bank an enabling ground in their states.

Just like the Zamfara State Government invested 1.5 billion Naira in *Ja'iz Bank* to boost the bank's capital base when a branch was opened in the state²⁶, other *sharī'ah* compliant states should follow suit because *sharī'ah* is more of caring for the welfare of the citizen than the application of criminal punishments for offences committed. It is only when a state takes care of the citizen that it has the right to challenge the citizen for being criminal.

Muslims should be enlightened on the benefit of banking with an Islamic bank and management of the bank should go on air to explain to the masses the various products operated in the Islamic bank and what it takes to be a member with the bank. The said orientation is to be in form of education for the masses because the system is new to the masses.

In conclusion, it is the strong belief of the author that if the bank is properly managed, a time will come when it will flourish in the country even more than the conventional banks that precede it in operation because no rational being will see a bank that doesn't take interest on a loan he takes and will choose to bank with the one that will take from him, such interest that could be more than the profit he made from the business on which he invested the money.

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